FARM CREDIT ADMINISTRATION
Washington, D. C.

SUMMARY OF CASES

RELATING TO

FARMERS' COOPERATIVE ASSOCIATIONS

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COOPERATIVE RESEARCH AND SERVICE DIVISION

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UNITED STATES SUPREME COURT UPHOLDS AGRICULTURAL MARKETING AGREEMENT ACT OF 1937

An action was brought by the Government to require compliance with Order No. 27 of the Secretary of Agriculture, for regulating the handling of milk in the New York City metropolitan area, issued pursuant to the Agricultural Marketing Agreement Act of 1937. The lower court held the Act unconstitutional, in part, and the Order invalid. United States v. Rock Royal Co-operative, 26 F. Supp.534. As the constitutionality of certain sections of an Act of Congress was one ground of the decision, an appeal was allowed directly to the Supreme Court where a reversal was obtained.

In discussing the occasion for the Order of the Secretary of Agriculture, the Supreme Court said:

> "Since these producers are numerous enough to keep up a volume of fluid milk for New York distribution beyond ordinary requirements, cut-throat competition even among them would threaten the quality and in the end the quantity of fluid milk deemed suitable for New York consumption. Students of the problem generally have apparently recognized a fair division among producers of the fluid milk market and utilization of the rest of the available supply in other dairy staples as an appropriate method of attack for its solution. Order No. 27 was an attempt to make effective such an arrangement under the authority of the Agricultural Marketing Agreement Act."

The Court explained the "minimum price" for milk, fixed by the Secretary, by saying:

> "It should be understood, however, that this minimum price is not the amount which the producer receives but the price level or so-called 'value' from which is calculated the actual amount in dollars and cents which he is to receive.
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> "By Article VI a uniform price is computed and it is this uniform price which the producer is actually paid by the proprietary (noncooperative) handlers. The uniform price is determined by a computation which in substance multiplies the amount of milk (classified according to its use) received by all handlers, less certain quantities of milk permitted to be deducted, by the minimum prices fixed by Article IV for the different classes of milk. From the result various payments and reservations are deducted and the remainder is divided by the total quantity of milk received. To equalize, handlers pay into the producer settlement fund. While much oversimplified the operation will be made clear by summarizing

the provisions of Article VII to require that handlers shall pay to the producer settlement fund the amount by which their purchased milk multiplied by the minimum prices for the various classes is greater than their purchased milk multiplied by the uniform price. When the handlers' purchased milk multiplied by the minimum prices is less than when it is multiplied by the uniform price, the producer settlement fund pays them the difference for distribution to their producers. These provisions give uniform prices to all producers, with exceptions to be herein stated, in accordance with the general use of milk for the preceding period."

In discussing the adoption of the Order, accomplished by a referendum of producers, the Court found that of 38,627 votes counted as valid, 87.1 percent were in favor of the issuance of the Order, and 12.9 percent were opposed. The Dairymen's League Cooperative Association, an intervening plaintiff, cast two-thirds of the favorable votes. In this connection the Court said:

"It is quite true that the League which itself cast two-thirds of the favorable votes was in a position to cast more than one-third of the total qualified vote against the Order. This arises from the provision of the Act, authorizing cooperatives to express the approval or disapproval for all of their members or patrons. This is not an unreasonable provision, as the cooperative is the marketing agency of those for whom it votes. If the power is in the Congress to put the order in effect, the manner of the demonstration of further approval is likewise under its control. These associations of producers of milk have a vital interest in the establishment of an efficient marketing system. This adequately explains their interest in securing the adoption of an order believed by them to be favorable for this purpose. If ulterior motives of corporate aggrandizement stimulated their activities, their efforts were not thereby rendered unlawful. If the Act and Order are otherwise valid, the fact that their effect would be to give cooperatives a monopoly of the market would not violate the Sherman Act or justify the refusal of the injunction."

A further contention in opposition to the Order was that the Act contained no statutory basis for those sections of the Order exempting cooperatives from the payment of the uniform price and authorizing payments to them from the producer settlement fund. The Court found that the earlier paragraphs of the Act

"provide for minimum prices to be paid by handlers to producers and associations of producers, subject to usual quality and location differentials not important here. These would require minimum prices to be paid by cooperatives when,

as here, they were handlers under the definition of the Order, were it not for the exception of these same cooperatives under subsection [8c(5)] (F): 'Nothing . . . shall . . . prevent a cooperative . . . from . . . making distribution thereof [net proceeds] . . . in accordance with the contract between the association and its producers.' This language specifically permits, indeed requires, the Order to except cooperatives from the requirement of paying minimum prices to producers. As the minimum price is paid to the producer through the payment of the uniform price, after equalization in the pool, there is authority in the Act to except the cooperative from the payment of the uniform price."

One of the defendants, a proprietary (noncooperative) handler, urged that as milk cooperatives were not required to pay producers a uniform price, a requirement that proprietary handlers pay the uniform price was unreasonably discriminatory and violative of the due process clause of the Fifth Amendment. The Supreme Court, however, recognized that cooperative associations are unique to a degree which justifies different treatment:

"The general characteristics of cooperatives are well understood. The Capper-Volstead Act defines such cooperatives as associations of producers, corporate or otherwise, with or without capital stock, marketing their product for the mutual benefit of the members as producers with equal voting privileges, restricted dividends on capital employed and dealings limited to 50 percent nonmember products. Different treatment has been accorded marketing cooperatives by state and Federal legislation alike. Indeed the Secretary is charged by this Act to 'accord such recognition and encouragement to producer-owned and producer-controlled cooperative associations as will be in harmony with the policy toward cooperative associations set forth in existing Acts of Congress, and as will tend to promote efficient methods of marketing and distribution.' These agricultural cooperatives are the means by which farmers and stockmen enter into the processing and distribution of their crops and livestock. The distinctions between such cooperatives and business organizations have repeatedly been held to justify different treatment. . . .

"The producer cooperative seeks to return to its members the largest possible portion of the dollar necessarily spent by the consumer for the product with deductions only for modest distribution costs, without profit to the membership cooperative and with limited profit to the stock cooperative. It is organized by producers for their mutual benefit. For that reason, it may be assumed that it will seek to distribute the largest amounts to its patrons.

"The commodity handled by a cooperative corresponds for some purposes to the capital of a business corporation. Either may cut sale prices below cost, one as long as its members will deliver, the other as long as its assets permit. When proprietary corporations lower sales prices, they naturally seek to lower purchase prices. Their profit depends on spread. On the other hand, the cooperative cannot pass the reduction. All the selling price less expense is available for distribution to its patrons. As its own members bear the burden of price cutting, it was reasonable to exempt it from the payment of the fixed price. The cooperative member measures his return by the market or uniform price the business handler pays. In commodities with the wide market of staple dairy products, quotations are readily available. If distributions do not equal open prices, the cooperators' reactions would parallel those of stockholders of losing businesses. Neither the Act nor the order protects anyone from lawful competition, nor is it essential that they should do so. We do not find an unreasonable discrimination in excepting producers' cooperatives from the requirement to pay a uniform price."

In answer to the argument that "the regulation 'of the price to be paid upon the sale by a dairy farmer who delivers his milk to some country plant'" was unauthorized because no interstate commerce was involved, the Court said:

"It is urged that the sale, a local transaction, is fully completed before any interstate commerce begins and that the attempt to fix the price or other elements of that incident violates the Tenth Amendment. But where commodities are bought for use beyond state lines, the sale is a part of interstate commerce. . . .

"The authority of the Federal government over interstate commerce does not differ in extent or character from that retained by the states over intrastate commerce. Since Munn v. Illinois, this Court has had occasion repeatedly to give consideration to the action of states in regulating prices. Recently, upon a reexamination of the grounds of state power over prices, that power was phrased by this Court to mean that 'upon proper occasion and by appropriate measures the state may regulate a business in any of its aspects, including the prices to be charged for the products or commodities it sells.'

"The power of a state to fix the price of milk has been adjudicated by this Court. . . . The power enjoyed by the states to regulate the prices for handling and selling commodities within their internal commerce rests with the Congress in the commerce between the states."

The purpose of the producer settlement fund was to provide an equalization pool through which each producer, dealing with a proprietary handler, received ultimately a uniform or weighted average price for his milk, irrespective of the manner of its use. In disposing of objections to this procedure, the Court declared:

> "The defendants' objection to the equalization pool . . . is to the alleged deprivation of liberty and property accomplished by the pooling requirement in taking away from the defendants their right to acquire milk from their patrons at the minimum class price, according to its use, and forcing the handlers to pay their surplus, over the uniform price, to the equalization pool instead of their patrons. This argument assumes the validity of price regulation, as such, but denies the constitutionality of the pooling arrangement because handlers are not at liberty to pay the producer in accordance with the use of the producer's milk but must distribute the surplus to others whose milk was resold less advantageously. . . .
>
> ". . . The pool is only a device reasonably adapted to allow regulation of the interstate market upon terms which minimize the results of the restrictions. It is ancillary to the price regulation, designed, as is the price provision, to foster, protect and encourage interstate commerce by smoothing out the difficulties of the surplus and cut-throat competition which burdened this marketing. . . . As the Congress would have, clearly, the right to permit only limited amounts of milk to move in interstate commerce, we are of the opinion it might permit the movement on terms of pool settlement here provided.
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> "Common funds for equalizing risks are not unknown and have not been considered violative of due process."

The defendant, Central New York Cooperative Association, a cooperative association of the agency type, claimed immunity from certain terms of the Order.

> "The asserted reason for its freedom from liability is that it is a cooperative composed of milk producers and distributes the milk of its members and others as agent.
>
> "The cooperative owns no farms. Its members are dairy farmers. By their contract they agree 'to deliver . . . all . . . milk produced . . . which said milk is to be marketed and distributed by the [cooperative] . . .' The latter 'agrees to pay . . . for the milk . . . a price . . . based upon the amount received . . . less the expenses . . .' Nonmembers'

milk is marketed under the same contract. The cooperative leases receiving and distributing facilities from a business corporation.

The milk is received by the cooperative at receiving plants and shipped to the city depot. It distributes through other business corporations which are wholly owned subsidiaries of the cooperative. These distributing subsidiaries use the leased physical facilities under verbal contracts with the cooperative. The cooperative receives the net amount from the sales and distributes to its patrons . . .

"Section 8c(5) (A) authorizes an order to classify milk and fix minimum prices which all handlers shall pay for milk purchased from producers. Section 8c(5)(C) authorizes the equalization pool and the handlers' payment to this settlement fund. It is urged that cooperatives which merely act as agents for their members are not included in handlers purchasing from producers. This is said to be definitely shown by the provisions of 8c(5)(F) providing that nothing contained in the subsection shall be construed to prevent a Capper-Volstead cooperative from making distribution to its 'producers in accordance with the contract.' The Order defines a handler as including a cooperative association 'with respect to any milk received from producers at any plant operated by such association or with respect to any milk which it causes to be delivered' to other handlers. Under the provisions of the Order, Article VII, Sections 8 and 9, cooperative handlers as other handlers equalize their purchases by payment into the producer settlement fund, even though they are not required to pay the uniform price to their producers by reason of the exception of Article VII, Section 1, and the provisions of 8c(5)(F). . .

"Cooperative contracts are of two general types, sale and agency. The Central New York Cooperative operates under the agency type.

"It is obvious that the use of the word 'purchased' in the Act, Section 8c(5)(A) and (C), would not exclude the 'sale' type of cooperative. When 8c(5)(F) was drawn, however, it was made to apply to both the 'sale' and 'agency' type without distinction. This would indicate there had been no intention to distinguish between the two types by (A) and (C). The section which authorizes all orders, Section 8c(1), makes no distinction. The orders are to be applicable to 'processors, associations of producers, and others engaged in the handling' of commodities. The reports on the bill show no effort to differentiate. Neither do the debates in Congress. The statutory provisions for equalization of the burdens of

surplus would be rendered nugatory by the exception of 'agency' cooperatives. The administrative construction has been to include such organizations as handlers. With this we agree. As here used the word 'purchased' means 'acquired for marketing.' Subsection (A) cannot be construed as freeing agents, cooperative or proprietary, from the requirement to account at the minimum prices for milk handled.

"As a corollary the contention is made also by Central Cooperative that no cooperative may be required to pay its surplus receipts over uniform prices into the equalization fund. This, too, is based upon a construction of Section 8c(5)(F) as permitting a cooperative to make settlement with its members in accordance with the terms of its own contract with them. If the cooperative members were freed of the burden of carrying their proportion of milk going to manufacturing use, the discrimination in their favor would be most strongly marked. Such a construction is not required. Cooperatives are covered by Section 8c(1) and (5)(A) and (B), and by the provisions of the Order, except as to the payment of the uniform price. Any payments below the uniform price fall on their members. We are of the view that the administrative construction is correct and that the 'net proceeds' of (F) refer to the result of the cooperative sales in the marketing area after complying with the equalization requirements."

The Order authorized the deduction from the milk involved in the equalization pool, in determining the net pool obligation of any handler, of "the quantity of milk received from the handler's own farm." The Central New York Cooperative Association took a position which evidenced its confusion in failing to distinguish between itself, as a cooperative association, and its individual producer members. In this connection, the Supreme Court said:

"We have determined that this cooperative, though marketing milk under an agency contract with its members, is a handler subject to the Act and Order. The cooperative argues that as its members, farmers, would not need to account to the pool for their personal sales to consumers, the cooperative, being utilized as an agent to market the farmers' milk, is under no obligation to contribute to equalization. As the cooperative does not have its own farm but is itself a handler under the Act, it must pay into the producer settlement fund."

The Supreme Court concluded its opinion by directing the specific enforcement of Order No. 27 and the enjoining of all defendants from further violation of the Order. United States of America v.

Rock Royal Co-operative, Inc., et al., decided June 5, 1939, 59 Supreme Court 993.

Attention is also called to the case of H. P. Hood & Sons, Inc., et al. v. United States et al., 59 Supreme Court 1019, decided June 5, 1939, wherein the Supreme Court upheld Order No. 4, as amended, of the Secretary of Agriculture, regulating the marketing of milk in the Boston, Massachusetts, area.

WAGE AND HOUR DIVISION INTERPRETS EXEMPTION OF AGRICULTURE AND EXEMPTIONS FOR PROCESSING AGRICULTURAL COMMODITIES

Exemption from the Wage and Hour Law for agriculture and exemptions for the processing of agricultural commodities are described in Interpretative Bulletin No. 14 of the Wage and Hour Division, United States Department of Labor, made public on August 21, 1939, by George A. McNulty, General Counsel of the Division. A press release relating thereto read, in part, as follows:

> "The bulletin contains a detailed explanation of the application of the Fair Labor Standards Act with respect to agriculture and operations bordering on agriculture, and was prepared for the guidance of the Wage-Hour Division in administering the law.
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> "'The Wage and Hour Law does not cover agriculture,' Administrator Elmer F. Andrews pointed out. 'The law never has covered farming, and none of the amendments proposed during the session of Congress just ended would have brought farming under the provisions of the Fair Labor Standards Act. This interpretative bulletin, the fourteenth of a series, has been issued to indicate the manner in which the Division will deal with the many problems that arise in the flow of farm products from the farm where they are grown.'
>
> "Three subjects are dealt with in the bulletin: complete exemption from the wage and hour provisions of the Act for employees engaged in 'agriculture'; total or partial exemptions from the hours provisions of the Act applicable to employees of employers engaged in certain operations upon agricultural or horticultural commodities, dairy products, poultry or livestock; complete exemption from the wage and hour provisions for persons employed within the 'area of production' in certain operations with respect to agricultural or horticultural commodities or employed in making dairy products."

INTERFERING WITH ORGANIZATION OF PRODUCER-CONTROLLED COOPERATIVES PROHIBITED

On July 24, 1939, the Federal Trade Commission issued a press release reading as follows:

"Under an order issued by the Federal Trade Commission, Gold Medal Farms, Inc., New York milk distributor, and two of its employed officials, are directed to cease and desist from certain unfair competitive practices in connection with the purchase of milk from producers in the New York milk shed.

"The order directs that they discontinue deceiving, coercing or intimidating New York or Vermont producers from whom they purchase or receive or may hereafter purchase or receive milk, in the efforts of such producers to form producer-controlled cooperatives; that they cease threatening reprisals or interfering in any way with the organization of cooperative associations of milk producers; that they discontinue disparaging and misrepresenting producers' cooperative bargaining agencies, and cease controlling or dominating the Washington and Rensselaer Counties Producers' Cooperative Association, Inc., or any other producers' cooperative associations.

"Gold Medal Farms, with its principal office at 1157 East 156th St., New York, is engaged in buying milk and cream at its Buskirk, N. Y., creamery, which it sells and delivers to the wholesale and retail trade in New York City. Its New York plant has a capacity for pasteurizing 220,000 pounds of milk a day, and its receiving station at Buskirk is one of the largest in the State.

"Findings are that Joseph Fromm, general manager of Gold Medal Farms, and Paul Steffin, superintendent of the Buskirk station, the officials named as respondents, control the policies of Gold Medal Farms in its relations with milk producing patrons.

"Findings of the Commission are that both the Federal and New York State Governments, through various agencies, made investigations and reports as to the best methods of stabilizing the dairy industry in the New York milk shed to secure an adequate and proper milk supply for the New York metropolitan area and to assure a fair return to milk producers in the New York milk shed, and it was recommended that the formation of producer-controlled cooperatives be encouraged.

"The Rogers-Allen Milk-Stabilization Act, enacted by the New York State legislature in May, 1937, provides for establishment of producers' and dealers' bargaining agencies, and the Metropolitan Cooperative Milk Producers' Bargaining Agency, Inc., Syracuse, N. Y., was organized, the Commission finds, with one of its primary objectives being to act as a milk producers' bargaining agency under the provisions of the Rogers-Allen law. It is the only such agency created under New York State laws whereby more than one producers' cooperative may join other cooperatives in joint bargaining.

"The findings continue that close to 48,000 of the approximately 62,500 producers in the New York milk shed are affiliated with the Producers' Agency through 90 cooperative associations in New York and other States comprising this milk shed; that the number of affiliates has been as high as 50,000, and that dealers and distributors in the New York area organized the Metropolitan Milk Distributors' Bargaining Agency to bargain collectively with the Producers' Agency, under provisions of the Rogers-Allen Act.

"Findings are that efforts of the Producers' Agency to help farmers form and maintain local cooperatives which could join the agency, met with dealer opposition, and that at meetings held at Johnsonville and Eagle Bridge, N.Y. in the Summer of 1937, the respondents did their utmost to prevent the producers selling milk to Gold Medal Farms from forming a producer-controlled cooperative to become affiliated with the Producers' Agency. The respondents' representatives are found to have harangued the producers with arguments against forming the cooperative, making false and disparaging statements concerning the Agency, its members, its objectives and the character of its representatives, and putting producers in fear of losing the Gold Medal Farms as a market for their milk if they formed such a cooperative.

"Among representations found to have been made by the respondents and their representatives were statements that the Producers' Agency was dominated by the Dairymen's League and that the League's certificates of indebtedness were worthless. The findings declare that the Agency's by-laws prevent control by the League and that the League's certificates of indebtedness are not worthless, but are of substantial value and readily marketable.

"The Commission finds that the respondents induced New York and Vermont producers to form the Washington and Rensselaer Counties Producers' Cooperative Association in 1937 through which to sell directly to Gold Medal Farms; that they held

out to producers exaggerated promises of higher prices than those received by producers belonging to cooperatives which were members of the Agency, and that they also put them in fear of losing their market if they would not join the cooperative sponsored by Gold Medal Farms. The result was, the findings continue, that more than 400 patrons of the respondents joined the Washington and Rensselaer Cooperative and that such producer-members had little, if any, voice in its management.

"These acts and practices, the Commission finds, have a tendency to coerce, intimidate and deceive Vermont and New York producers selling to Gold Medal Farms, and have prevented them from exercising their free choice in deciding whether or not to form a producer-controlled cooperative association to join the Agency, thereby depriving such producers of the higher prices which would normally result from a single selling agency in control of all milk produced in the New York milk shed, and giving Gold Medal Farms, Inc., a competitive advantage over dealers who do not so unfairly interfere with their producers. These acts and practices are found to have a tendency to encourage unfair competition among dealers and to reduce the price paid by them to their producers for milk below the cost of production, and thus to threaten the quality and quantity of milk deemed suitable for consumption in the New York metropolitan milk market, with resulting injury to the consuming public.

"The respondents are ordered to cease and desist from (1) deceiving, coercing or intimidating any milk producers from whom they purchase or receive, or may hereafter purchase or receive, milk, with the intent or result of preventing such producers from organizing, joining or becoming affiliated with any milk producers' cooperative association; (2) deceiving, coercing or intimidating such producers with the intent or result of causing such producers to assist in organizing, joining or becoming affiliated with any milk producers' cooperative organization; (3) threatening reprisals against any such producers, as a penalty for attempting to assist in forming any milk producers' cooperative organization; (4) interfering by means of deception, coercion or intimidation with the free and unimpeded exercise of choice by such producers, in their determination as to whether they should organize or join any producers' cooperative organization; (5) interfering with the free and unimpeded choice of any milk producers' cooperative association in its determination of whether it shall become affiliated in any manner or form with the Metropolitan Cooperative Producers' Bargaining Agency, Inc., or any other cooperative agency authorized by law; (6) making or causing to be made any false or disparaging statements

concerning the Metropolitan Cooperative Milk Producers' Bargaining Agency, Inc., or any other lawfully organized cooperative, and (7) controlling, dominating, or interfering in any manner with the organization, management, control or operation of the Washington and Rensselaer Counties Producers' Cooperative Association, Inc., or any other milk producers' cooperative association or agency authorized by law, with the purpose, intent or result of preventing the producer-members, officers or directors of such a cooperative from exercising their free and unimpeded judgment as to its organization, management, control or operation."

(3380)

FOR INCOME TAX EXEMPTION, NONMEMBERS MUST BE TREATED SAME AS MEMBERS

Without having made an application for exemption from income taxation (Internal Revenue Form 1028) and relying apparently on the assumption that it was exempt from such income taxation, a cooperative association did not file a return for the year 1928. Some time later the Commissioner of Internal Revenue assessed a tax for the year 1928 of $1,065.93 and a penalty of $266.48 for failure to file a return, making a total of $1,332.41.

The business of the association, conducted with both members and nonmembers, consisted of operating a grain elevator, a feed store, and a general merchandising store; the handling of machinery supplies and repairs; and the purchase, sale, and shipping of grain and other farm products. Under its system of operation, purchases were made at market price less the estimated cost of handling, and sales were made at cost plus the estimated cost of handling. Insofar as the estimates exceeded actual costs the association accumulated a cash balance, and on such a cash balance the Commissioner of Internal Revenue assessed the tax.

The association claimed exemption from taxation on two principal grounds: (1) that the accumulated cash balance was not income to it, within the contemplation of the Sixteenth Amendment to the Constitution, but was rather "accumulated savings" of its patrons; (2) that even if the accumulated cash balance were its income, the association nevertheless was exempt from taxation under the provisions of section 103(12) of the Revenue Act (1928) relating to the exemption of farmers' associations organized and operated on a cooperative basis, for the reason that it was properly organized under a State statute which authorized the distribution of earnings in part, or wholly, on the basis of the amount of property bought from or sold to members.

The bylaws of the cooperative association provided for the creation of a surplus, for the payment of 8 percent annual dividends to shareholders, for the creation of a "contingent reserve fund," and, finally, that all remaining net profits should be prorated to stockholders in proportion to the amount of business they had done with the corporation during the business year.

The Circuit Court of Appeals, in holding that the accumulated balance in the hands of the association was its own property and that the association was a separate legal entity, said:

> "Clearly this money is property of the corporation as genuinely and truly as is the grain elevator or the stock of merchandise owned by it. While those who might be entitled to patronage dividends have, in a sense, an interest in the money, it is a character of interest not greater, if as great, as that of a stockholder in an ordinary corporation. Such interest never ripens into an individual ownership or right of ownership until and if a patronage dividend be declared. Fruit Growers' Supply Co. v. Commissioner, 56 F.(2d) 90, 93 (C.C.A.9); and see Penn Mutual Life Ins. Co. v. Lederer, 252 U.S. 523, 40 S. Ct. 397, 64 L. Ed. 698. Until such declaration, the money is the property solely of the petitioner."

The accumulated cash balance was therefore "income" of the cooperative, within the meaning of the Sixteenth Amendment to the Constitution, and was taxable unless exempted by the provisions of the Revenue Act.

The Court disposed of the contention of the association that it was properly organized as a cooperative within a State statute and was therefore exempt from paying income taxes under section 103(12) of the Revenue Act (1928) relating to the exemption of farmers' associations by saying:

> "Whether a person is within the federal taxing statutes depends solely upon those statutes. State laws do not alter this."

As has been previously stated, the business of the association was conducted with both members and nonmembers. The bylaws of the association, however, required the distribution of patronage dividends "to stockholders in proportion to the amount of business they have done with [the] corporation during [the] business year." No provision was made for patronage returns to nonmembers. In showing the features of the organization and operation of the association which prevented it from qualifying as exempt from the payment of income taxes, the Court pointed out the requirements of the Revenue Act in the following language:

"* * In marketing the products 'of members or other producers,' there shall be turned back to them 'the proceeds of sales, less the necessary marketing expenses' on the basis stated. A similar requirement is that sales to patrons -- both 'members or other persons' -- shall be 'at actual cost, plus necessary expenses.'"

The Court added:

"The thing here important is the requirement (both as to marketing and as to sales) that nonmember patrons are to be dealt with on a non-profit basis. A substantial part of petitioner's business -- both as marketing agent and as merchandise seller -- was with nonmember patrons.

"Petitioner could not accord to nonmember patrons this non-profit treatment required by the act because of the structure of its organization. Article IV of its bylaws entirely and effectively prevented petitioner from according to nonmember patrons the treatment required by the section. After providing (in sections 1 to 4 of the by-laws) for several allowable dispositions of 'net profits' to surplus, stock dividends, and contingent reserve fund, this article (section 5) provides that: 'All remaining net profits, shall be pro-rated to stockholders in proportion to the amount of business they have done with corporation during business year.' Thus, nonmember patrons were wholly excluded from any possible participation."

The Court thus held that the cooperative association failed to meet the requirements of the Revenue Act for exemption from the payment of income tax. Farmers Union Cooperative Company, etc., v. Commissioner of Internal Revenue, 90 F.(2d) 488, affirming an order of the Board of Tax Appeals, 33 B.T.A. 225.

EXEMPTION OF FARMERS FROM TEXAS ANTITRUST LAW UPHELD

In the case of Ex parte Herbert Tigner, decided June 23, 1939, the Court of Criminal Appeals of Texas, the court of last resort in Texas for criminal cases, held that a provision in the criminal antitrust statute of that state, reading in part as follows:

"Article 1642. No provision of this law shall apply to agricultural products or live stock while in the hands of the producer or raiser,"

did not operate to cause such statute to violate the equal protection clause of the Fourteenth Amendment of the Constitution of the United States. Tigner was indicted for entering into an alleged

conspiracy to fix the retail price of beer in violation of the antitrust statute, and was arrested and placed in jail. When he attempted to obtain his freedom in a habeas corpus proceeding, the trial court refused to order his release. Tigner appealed.

In affirming the action of the lower court the appellate court said:

> "It is the contention of appellant that the statute under which he is indicted is repugnant to the equal protection clause of the Fourteenth Amendment of the Constitution of the United States because of Article 1642, . . . which excludes from the operation of the statute agricultural products and live stock while in the hands of the producer or raiser. . . .
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> " . . .
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> "In the case of Connolly v. Union Sewer Pipe Company, 184 U. S. 540, 46 L. ed. 679, which was decided more than thirty-seven years ago, the Supreme Court of the United States held that a trust statute of the State of Illinois was invalid because it excluded from its operation 'agricultural products or live stock while in the hands of the producer or raiser.' If the decision in that case is to be regarded as determinative, appellant should be ordered discharged without further discussion of the question presented in this appeal."

However, after an extensive review of various cases upholding statutes which excluded one or more classes from their operations, the Court concluded that:

> "While the rules by which the reasonableness of a classification adopted by the Legislature in dealing with economic policy may not change, it can not be said that supervening economic conditions may not render a classification reasonable which, under the conditions prevailing at a remote time, would have been purely arbitrary. If a classification declared to be arbitrary and unreasonable more than thirty-seven years ago should be taken to foreclose legislative adoption of the same classification in an effort to deal with economic problems affecting the prosperity and general welfare of the people of the State, then it may be said that the police power of the State is so circumscribed by the Fourteenth Amendment as that the legislature is powerless to adequately deal with the problems resulting from changing economic conditions. It is in view of the supervening economic conditions since 1902 that we have not regarded the decision in the Connolly Case as determinative of the question

in the case at bar. In reaching the conclusion that it should be again considered, we are cognizant of our duty to give effect to the decisions of the Supreme Court of the United States involving the application of the Fourteenth Amendment. We have been hesitant in reaching the conclusion that a discussion of the question should be renewed. But with due deference to the superior authority of the Supreme Court, we have felt that the importance of the question involved in this appeal to the people of the State makes it our imperative duty in deciding the case to give it fresh consideration. . . .

"Returning to the case before us, it is manifest that the whole statute is one concerned with economic policy. It is a declaration of mala prohibita as to combinations to control the price of commodities by merchants, traders, manufacturers; not, however, as to combinations of farmers and stock raisers in dealing with their products in hand which they have produced or raised. As pointed out in the dissenting opinion of Mr. Justice McKenna in the Connolly Case, the class included in the statute is composed of merchants, traders, manufacturers, all engaged in commercial transactions, who generally are congregated in the cities and towns, while the excluded class is composed of farmers and stock raisers who are scattered over farms and ranches. It was largely due to the difference of these situations that Mr. Justice McKenna expressed the opinion that the classification adopted by the Illinois Legislature, in dealing with the economic policy of that State, was permissible under the equal protection clause of the Fourteenth Amendment. Be that as it may, it is observed that the Fourteenth Amendment was not designed to interfere with the power of the State to deal with economic problems to the end that the general prosperity and well-being of the people might be promoted.

" . . .

"Presumably the [Texas] legislature was moved by economic considerations in excepting agricultural products and live stock from the provisions of the statute. Indeed, the economic conditions to which reference has been made would seem to fully justify the conclusion that there was reasonable ground for believing that there were public considerations for making the exception. The legislature, in making the classification, was entitled to consider prevailing economic conditions and the differences between the classes in their relation to the ultimate object of the statute, which was the promotion of the general prosperity. We think that in view of the prevailing economic conditions at the time of the enactment of the statute it cannot be said that the distinction made is unreasonable."

STATEMENTS RENDERED TO MEMBERS CONSTITUTED ACCOUNTS STATED

Plaintiff and others, as vendors, entered into a sale contract of 240 acres of orchard land. The purchasers agreed therein that all fruit would be marketed through the defendant, Apple Growers Association, of Hood River, Oregon, and that the Association should credit all of said fruit to a special account for the vendors of the land and should pay all proceeds from the sale of such fruit to a named bank as escrow agent. The Association was not a party to the sale contract of the orchard land. The purchasers of the land, who are hereinafter designated as "the purchasers," were not made parties to the court proceeding. At least one of "the purchasers" was at all times a grower member of the defendant association, and the fruit involved in the suit was delivered by "the purchasers" to the defendant under and by virtue of such grower member's marketing contract.

All grower members of defendant association were required to enter into marketing contracts with it. The plaintiff claimed the Association had made unauthorized deductions under the marketing contracts, which had redounded to his loss under the sale contract of the orchard land. The lower court dismissed the suit. From such decree of dismissal the plaintiff appealed.

The Supreme Court of Oregon stated the plaintiff's position in the following language:

> "Plaintiff contends that there were unauthorized deductions by defendant from the proceeds of the deliveries made under these [marketing] contracts. Plaintiff also contends that moneys, which should have been paid for the fruit delivered under these [marketing] contracts, were wrongfully applied to the expense of maintaining a cannery and a cider or vinegar factory, and to the payment of interest. Plaintiff also asserts that there was a surplus of money withheld by defendant, which should have been paid to the grower members."

In determining that the members bylaws of the Association were a part of the marketing contract between "the purchasers" and the defendant, the Supreme Court said:

> ". . . In these marketing contracts the representative of the parties, whom we designate as 'the purchasers,' is called the grower and defendant is designated as 'the association.' These marketing contracts contain the following paragraph:

"'The Grower agrees to haul and pack his fruit in accordance with the methods and rules prescribed by the Association and to deliver the same free of expense to the Association at Hood River -- (or if delivered to any other shipping point, freight and switching charges to Hood River to be borne by the Grower) -- at such time as may be designated by the Association. The grower further agrees to comply with and conform to all of the rules, regulations and requirements of the Association.' (Italics supplied.)

"We think that the final sentence in the above quoted paragraph of 'the purchasers' contract with defendant expressly incorporates as part of said growers' contracts the pertinent provisions of the members by-laws of defendant. Moreover, we are unable to avoid the conclusion that all grower members, including the parties designated herein as 'the purchasers', are bound by the provisions of the members by-laws of defendant by reason of their relationship to defendant as grower members.

"At best, plaintiff is in the position of a successor in interest of 'the purchasers' and hence is likewise bound not only by the terms of the contracts existing between 'the purchasers' and defendant, but also by the terms and provisions of defendant's members by-laws."

The Court then proceeded to examine the members bylaws and found a provision creating "a permanent fund of an amount equal to from nothing to five cents per package per annum on all fruit handled . . ." which was to be "known as the 'Building and Equipment Fund,' and . . . shall be used exclusively for the purpose of or paying for property, . . . and no portion of said fund shall be paid out in any other manner or for any other purpose than as stated herein." In respect to the plaintiff's claim, the Court declared:

"There is nothing in the record disclosing that any money, which should have been paid to 'the purchasers' for the fruit in suit, was treated as belonging to the Building and Equipment Fund Account.

"The argument is presented that defendant had no source of revenue except that which was derived from crop sales. This is answered by the obvious statement that defendant had its credit, sometimes used to the extent of $1,000,000; and defendant also had its Building and Equipment Fund. We are not able to follow defendant's argument that it is impossible for defendant to suffer loss. To us it is clear, when defendant embarks in the canning industry and the manufacture of cider and vinegar, borrowing several hundred thousands of dollars for that purpose, that depreciation in the value of its

plants alone may cause substantial loss to the defendant. That such a loss may or may not be passed on to and assumed by its members is beside the point. To us it is clear that in such a contingency the defendant will have suffered a loss, even such a loss as to bring about a final liquidation; but we think that this question is not presented here. The question here is whether funds, which should have been credited to the purchasers, have been diverted to the Building and Equipment account. The defendant markets the products of its members in pools. That means that all of a given kind of fruit received during a season is treated, handled and marketed separately from other kinds and varieties. There may be a pool, for instance of Gravenstein apples, another of Comice pears, etc.

"There is some evidence tending to show that ordinarily in the usual course returns upon the respective pools are available to the members within six months, and it is argued that where, as in the case at bar, a longer time has elapsed, the delay may be attributed to the use of defendant's money in paying interest; but we think that in that respect we would be entering into the realm of conjecture if we held in accordance with such argument.

"It appears that advances were made by defendant to the growers in larger sums than the market thereafter justified. It also appears that defendant had a large stock on hand of unsold fruit products. An adjustment of these two items would materially reduce if not entirely efface the alleged loss claimed by plaintiff to have been sustained by defendant in operating its cannery and its cider and vinegar plants.

"To illustrate the matter of advances, defendant's witnesses testified to the effect that approximately 75% of the estimated return was the amount of the usual advance. To enable defendant to make advances prior to receipts from sales, defendant would borrow from the bank and later, as proceeds from sales were received, in liquidating the pools, defendant withheld the amounts previously advanced. In 1929, defendant advanced $8.00 per ton to participating members on canning apples and from $10 to $50 per ton on canning pears dependent on grade.

"These preseason estimates of returns were unjustified by the amounts actually realized and the result was that, when the pools were liquidated, the participating members owed the defendant instead of defendant owing them. . . . It is obvious these . . . items in defendant's assets more than offset the amount alleged by plaintiff to comprise an operating loss.

". . .

"No good purpose can be served by a further discussion of this phase of the case except to say that plaintiff has not proved that any funds were wrongfully diverted in connection with the cannery and cider and vinegar factory.

". . .

"It is an admitted fact that defendant deducted from the proceeds of the fruit crops in suit, for the nine years involved, the total sum of $16,977.69 for its building and equipment fund. That is less than four cents upon each of the 435,114 packages delivered by 'the purchasers.' The members by-laws authorize a deduction of from 'nothing to five cents per package'. Plaintiff has no ground of recovery in that respect."

The Court concluded its opinion with the following statement of the effect of submission of comprehensive statements of account each year to members:

"Notwithstanding our discussion of the facts, we think that the rendition of statements each fiscal year to plaintiff and 'the purchasers' and plaintiff's failure to object to or protest against such statements of account within a reasonable time thereafter constitute an account stated as to the transactions therein involved. . . .

"Plaintiff vigorously insists that there has been no account stated between plaintiff and defendant. . .

". . .

"In the case at bar the pool statements, that is, statements with respect to the various pools accompanied the duplicate ledger sheets. The debits charged appear plainly upon the pool statements with respect to handling, advertising, storage, operating charges, and building and equipment fund. The evidence discloses that these pool statements and ledger sheets were rendered to plaintiff when the pools were closed and some of them were introduced by plaintiff as exhibits herein. . . ."

Davidson v. Apple Growers Association, 79 Pac. (2d) 991, decided June 7, 1938, by the Supreme Court of Oregon.